

ALTERNATIVE FORECASTS

Global Insight has assigned a 55% probability of occurrence to its June 2004 baseline forecast of the U.S. economy. The major features of this forecast include:

- Real GDP increases 4.9% in 2004, 3.8% in 2005, 2.9% in 2006, and 3.4% in 2007;
- U.S. nonfarm employment grows 1.2% in 2004, 2.1% in 2005, 1.4% in 2006, and 1.1% in 2007;
- the U.S. civilian unemployment rate falls gradually from 5.5% in 2004 to 5.3% in 2007;
- inflation is 2.7% in 2004, 1.6% in 2005, 1.3% in 2006, and 1.9% in 2007;
- the real net export deficit grows from \$532 billion in 2003 to \$441 billion in 2007.

The *Optimistic* and *Pessimistic* alternative forecasts are broad mirror images of one another relative to the *Baseline Scenario*. In the *Optimistic Forecast* inflation is lower and growth is higher than in the baseline. Inflation is higher and growth is lower in the *Pessimistic Scenario*. These bandwidths exist in both the short and long runs. Mainly, they reflect different assumptions about productivity, foreign economic growth, and the dollar's strength.

OPTIMISTIC SCENARIO

The *Optimistic Scenario* has been assigned a 20% probability of occurrence. In this *Scenario*, total factor productivity is stronger than in the baseline, and this has several positive impacts. It is the main reason why economic and employment gains are higher and inflation and budget deficits are lower than in the baseline. It also helps strengthen the dollar, which helps keep a lid on inflation. This *Scenario* also assumes both developing and industrialized countries grow faster than in the baseline. This boosts U.S. exports, which helps shrink the merchandise trade deficit faster than in the baseline. In addition to the already mentioned assumptions, oil prices are expected to be lower and construction is expected to be higher.

These assumptions help paint a rosier picture for the U.S. economy. For example, real GDP advances 5.4% in 2004 and 4.8% in 2005. In comparison, real output was slated to increase 4.9% in 2004 and 3.8% in 2005 in the *Baseline Scenario*. Although economic growth and labor markets are stronger than in the baseline, forecasted inflation is actually lower thanks to the stronger dollar and the higher productivity growth. The lower inflation rate allows the Federal Reserve to keep its federal funds rate below the baseline value. It should also be pointed out that the assumed higher total productivity growth raises the bar for economic performance. Namely, potential GDP is higher than its baseline counterpart.

The higher U.S. productivity presents a mixed outlook for Idaho. It allows the U.S. economy to grow faster without inflation, which is a plus for Gem State employment. Specifically, nonfarm employment advances a healthy 1.5% this year, 2.0% next year and in 2006, and 2.1% in 2007. As a result, Idaho nonfarm employment is 617,738 in 2007, which is about 500 higher than in the *Baseline Forecast*. However, the higher productivity dampens unit labor cost, which lowers Idaho wage growth. The lower wage growth has a cascading effect on several components of Idaho personal income. As a result, Idaho nominal personal income is lower than its baseline counterpart. Interestingly, even after adjusting for inflation, Idaho personal income is still lower in this *Scenario* than in the *Baseline Scenario*.

IDAHO ECONOMIC FORECAST
BASELINE AND ALTERNATIVE FORECASTS
JULY 2004

	BASELINE				OPTIMISTIC				PESSIMISTIC			
	2004	2005	2006	2007	2004	2005	2006	2007	2004	2005	2006	2007
GDP (BILLIONS)												
Current \$	11,766	12,426	12,989	13,687	11,823	12,561	13,013	13,649	11,753	12,385	12,969	13,628
% Ch	7.1%	5.6%	4.5%	5.4%	7.6%	6.2%	3.6%	4.9%	7.0%	5.4%	4.7%	5.1%
2000 Chain-Weighted	10,909	11,320	11,652	12,043	10,958	11,487	11,799	12,206	10,886	11,176	11,379	11,649
% Ch	4.9%	3.8%	2.9%	3.4%	5.4%	4.8%	2.7%	3.4%	4.7%	2.7%	1.8%	2.4%
PERSONAL INCOME - CURR \$												
Idaho (Millions)	37,448	39,342	41,539	43,907	37,323	38,872	40,730	42,638	37,578	39,951	42,781	45,857
% Ch	5.8%	5.1%	5.6%	5.7%	5.4%	4.2%	4.8%	4.7%	6.1%	6.3%	7.1%	7.2%
U.S. (Billions)	9,733	10,273	10,809	11,425	9,748	10,334	10,812	11,360	9,732	10,257	10,817	11,455
% Ch	5.7%	5.6%	5.2%	5.7%	5.9%	6.0%	4.6%	5.1%	5.7%	5.4%	5.5%	5.9%
PERSONAL INCOME - 2000 \$												
Idaho (Millions)	34,780	35,942	37,360	38,654	34,689	35,729	37,068	38,150	34,833	36,008	37,536	39,207
% Ch	3.5%	3.3%	3.9%	3.5%	3.2%	3.0%	3.7%	2.9%	3.6%	3.4%	4.2%	4.5%
U.S. (Billions)	9,040	9,385	9,722	10,059	9,060	9,498	9,840	10,164	9,021	9,245	9,491	9,794
% Ch	3.4%	3.8%	3.6%	3.5%	3.6%	4.8%	3.6%	3.3%	3.2%	2.5%	2.7%	3.2%
TOTAL NONFARM EMPLOYMENT												
Idaho	581,463	591,493	603,784	617,212	581,424	592,934	604,777	617,738	581,423	590,681	601,707	615,534
% Ch	1.6%	1.7%	2.1%	2.2%	1.5%	2.0%	2.0%	2.1%	1.5%	1.6%	1.9%	2.3%
U.S. (Thousands)	131,492	134,195	136,040	137,580	131,810	135,522	137,773	139,271	131,389	133,285	134,027	134,497
% Ch	1.2%	2.1%	1.4%	1.1%	1.4%	2.8%	1.7%	1.1%	1.1%	1.4%	0.6%	0.4%
GOODS PRODUCING SECTOR												
Idaho	102,004	101,249	100,863	101,206	102,343	103,750	102,925	103,289	101,862	100,101	98,260	97,722
% Ch	-0.4%	-0.7%	-0.4%	0.3%	0.0%	1.4%	-0.8%	0.4%	-0.5%	-1.7%	-1.8%	-0.5%
U.S. (Thousands)	21,924	22,238	22,388	22,448	21,978	22,684	22,968	22,981	21,905	22,010	21,617	21,131
% Ch	0.5%	1.4%	0.7%	0.3%	0.7%	3.2%	1.3%	0.1%	0.4%	0.5%	-1.8%	-2.3%
NONGOODS PRODUCING SECTOR												
Idaho	479,460	490,244	502,921	516,006	479,081	489,184	501,851	514,449	479,561	490,581	503,448	517,812
% Ch	2.0%	2.2%	2.6%	2.6%	1.9%	2.1%	2.6%	2.5%	2.0%	2.3%	2.6%	2.9%
U.S. (Thousands)	109,567	111,957	113,652	115,132	109,832	112,839	114,804	116,290	109,484	111,275	112,409	113,366
% Ch	1.3%	2.2%	1.5%	1.3%	1.6%	2.7%	1.7%	1.3%	1.3%	1.6%	1.0%	0.9%
SELECTED INTEREST RATES												
Federal Funds	1.3%	2.8%	3.5%	3.5%	1.3%	2.7%	3.0%	3.0%	1.3%	3.2%	5.5%	6.6%
Bank Prime	4.3%	5.8%	6.5%	6.5%	4.3%	5.7%	6.0%	6.0%	4.3%	6.2%	8.5%	9.6%
Existing Home Mortgage	6.1%	6.8%	6.8%	6.8%	6.0%	6.5%	6.2%	6.2%	6.1%	7.3%	8.3%	8.8%
INFLATION												
GDP Price Deflator	2.1%	1.8%	1.6%	2.0%	2.1%	1.4%	0.9%	1.4%	2.2%	2.6%	2.8%	2.7%
Personal Cons Deflator	2.2%	1.7%	1.6%	2.2%	2.1%	1.4%	0.9%	1.4%	2.4%	2.8%	2.7%	2.6%
Consumer Price Index	2.7%	1.6%	1.3%	1.9%	2.6%	1.0%	0.7%	1.5%	2.9%	2.8%	2.4%	2.3%

Forecast Begins the FIRST Quarter of 2004

PESSIMISTIC SCENARIO

The assigned 25% probability of occurrence for the *Pessimistic Scenario* is marginally higher than that of the *Optimistic Scenario*. This alternative assumes there is less spare global economic capacity than in the baseline. The reason for this is rapid technological advances have rendered much of the currently idle capacity obsolete, but this capacity remains on the books nonetheless. Higher oil prices dampen Asian economic growth. European economic growth is stunted by the stubborn adherence to anti-growth regulatory and social policies. Although global growth slows, the dollar weakens as higher commodity prices cause the U.S. import bill to rise and the current account deficit to widen. As these price pressures mount, businesses raise their prices, causing inflation to accelerate.

The higher inflation causes the Federal Reserve to aggressively tighten. Between autumn 2005 and the end of 2006, the federal funds target rate rises from 4.0% to 7.5%. This strong medicine proves successful at staving off inflation, but it comes with a few negative side effects. The economy does not sink into a recession, but fails to narrow the gap between real and potential GDP. Under these circumstances, the U.S. unemployment rate actually deteriorates from 5.6% in 2004 to 6.7% in 2007. In the baseline, the unemployment rate gradually drops from 5.5% to 5.3% over this same period. The weaker economy takes a toll on federal finances. Namely, the federal budget deficit (unified basis) swells to \$458 billion in 2007 in the *Pessimistic Scenario*, which is well above the baseline's \$269 billion deficit.

In this *Scenario*, the outlook for Idaho employment is weaker than in the *Baseline Scenario*, but the personal income forecast is stronger. Specifically, Idaho nonfarm employment advances 1.5% in 2004, 1.6% in 2005, 1.9% in 2006, and 2.3% in 2007. Both Idaho nominal and real personal income increase faster than their baseline counterparts. Nominal income increases by about 6.0% in both 2004 and 2005, then accelerates to about 7.0% in 2006 and 2007. Annual nominal income growth remains below 6.0% in the *Baseline Scenario*. Adjusting for inflation narrows the growth gap between pessimistic and baseline nominal personal income, but does not erase it. This is especially notable in 2006 and 2007, when real personal income growth rises by at least 4.0% in each year, but it is less than 4.0% in the baseline case.